[illegible] Court of the United States

October Term, 1993

BARCLAYS BANK PLC,
Petitioner,

v.

FRANCHISE TAX BOARD,
An Agency of the State of California,
Respondent.

COLGATE-PALMOLIVE COMPANY,
Petitioner,

v.

FRANCHISE TAX BOARD,
An Agency of the State of California,
Respondent.

On Writ of Certiorari to the Court of Appeal of the State of California for the Third Appellate District

BRIEF [illegible] AMICI CURIAE THE STATE OF [illegible] AND THE STATES OF ARKANSAS, [illegible] MAINE AND RHODE ISLAND IN SUPPORT OF RESPONDENT FRANCHISE TAX BOARD

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QUESTION PRESENTED

Whether worldwide combined reporting may be constitutional applied to foreign-based and domestic-based unitary business enterprises under this Court's dormant Commerce Clause analysis?

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On Writs of Certiorari to the Court of Appeal of the State of California in and for the Third Appellate District

BRIEF OF AMICI CURIAE BY THE STATE OF NEW MEXICO AND THE STATES OF ARKANSAS, COLORADO, IDAHO, MAINE AND RHODE ISLAND IN SUPPORT OF RESPONDENT FRANCHISE TAX BOARD

INTEREST OF AMICI CURIAE

Amici are States which compute the individual tax liabilities of multijurisdictional business under the "unitary

business principle." Amici have a direct interest in the application of this Court's dormant Commerce Clause analysis to the question of what foreign source income of domestic corporate taxpayers can be considered in determining the amount of income which can be properly included in the taxpayer's apportionable tax base. This interest becomes greater each year with the continuing internationalization of the United States economy and the economy of each of the States. All of the Amici States, like California, employ accounting practices based on the formulary apportionment principle embodied in the Uniform Division of Income for Tax Purposes Act (UDITPA), 7A Uniform Laws Annotated 331 (West 1985). Many of these States include in their determination of a corporation's apportionable income interest, royalties, dividends and similar payments from that corporation's foreign subsidiaries ("foreign source" income). Taxpayers in a number of States have challenged the inclusion of this income in the apportionable bases, on the theory that the income, or the income payor, may have been subject to taxation by foreign jurisdictions under arm's-length accounting principles. *See, e.g., NCR Corporation v. Commissioner of Revenue*, 438 N.W.2d 86 (Minn. 1989), *cert. denied*, 493 U.S. 848 (1989); *NCR Corporation v. Taxation and Revenue Department of the State of New Mexico*, 856 P.2d 982 (N.M.Ct.App.1993), *cert. pending*, S.Ct. No. 93-541.

In 1983, this Court rendered a milestone decision in the area of state corporate income taxation in the case of *Container Corporation of America v. Franchise Tax Board*, 463 U.S. 159 (1983). The *Container* decision settled the jurisprudence in this area. This Court's acceptance of the petitions by Barclays and Colgate has drawn that decision into

question. A decision adverse to California in these cases would likely unsettle what are now viewed as resolved issues. Reversal of *Container* will have significant ramifications for all states which will take several decades of litigation to sort out. Amici believe that the fundamental holding of *Container* — that "foreign-source" income of a unitary business may be included in the apportioned tax base — should be affirmed.

STATEMENT PURSUANT TO RULE 37

This brief is submitted pursuant to Rule 37.3 of this Court in support of Respondent Franchise Tax Board, State of California. Consent to the filing of this brief has not been requested from the parties because the Amici filing this brief are the Attorneys General of their respective States. Rule 37.5.

SUMMARY OF ARGUMENT

The actions of the Federal Government establish that the California tax at issue in these cases is constitutionally permitted without the need for a dormant Commerce Clause analysis. Amici, nonetheless, undertake such an analysis and show that under that analytical tool the tax also passes constitutional muster.

Dormant foreign Commerce Clause analysis has six distinct elements. In the circumstances of these cases, there is no question that the taxpayers are engaged in worldwide unitary businesses and that the application of the three-factor apportionment formula has resulted in a fair and proper tax being computed. It is apparently uncontested that the first

(nexus), second (fair apportionment), and fourth (fair relationship) elements are met.

With respect to the third element of dormant Commerce Clause analysis, discrimination, Amici argue that Petitioner Barclays' claims are not complaints of discrimination but demands that they be discriminated *in favor of* because of their foreign parentage and location. There is no basis for such a claim. Foreign-based businesses have a legitimate basis to claim equal treatment, but not to claim preferential treatment.

This Court's analysis in *Container* of the fifth element of dormant Commerce Clause analysis, multiple taxation, is applicable to both foreign-based and domestic-based businesses. In the field of income taxation, the risk of multiple taxation can only be eliminated by requiring a jurisdiction to forgo taxation completely. This solution is neither proper nor required.

The final element of dormant Commerce Clause analysis, "one voice," applies to invalidate a tax only when uniformity is essential and possible foreign retaliation is justified. Neither circumstance is present in these cases. Twenty years of discussions, negotiations and agreements with the United Kingdom establish this to be true.

The California tax remains, as this Court found it in *Container*, a "proper and fair tax" and should be sustained.

ARGUMENT

THE CALIFORNIA TAX AT ISSUE IN THESE CASES MEETS ALL THE REQUIREMENTS OF THIS COURT'S DORMANT COMMERCE CLAUSE ANALYSIS

A. Introduction

No treaty to which the United States is a party, and no statutory enactment of the United States, specifically prohibits the States from using the worldwide combined report (WWCR) accounting method with respect to either domestic-based or foreign-based corporations. To the contrary, there is compelling evidence which establishes the existence of a federal policy permitting the States to use WWCR. *Wardair Canada, Inc. v. Florida Department of Revenue*, 477 U.S. 1 (1986). This policy can be drawn by implication from the body of federal law. Under these circumstances, a dormant Commerce Clause analysis is not required. Nonetheless, for purposes of argument only, Amici proceed on the premise that this Court may undertake a dormant Commerce Clause analysis to determine whether the California tax at issue in these two cases is constitutionally permissible.

The Constitution of the United States provides that the Congress shall have the power "to regulate commerce with foreign nations, and among the several states, and with the Indian tribes;" Article I, Section 8, Clause 3. "The few simple words of the Commerce Clause . . . reflected a central concern of the Framers that was an immediate reason for calling the Constitutional Convention: the conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued

relations among the Colonies and later among the States under the Articles of Confederation." *Hughes v. Oklahoma*, 441 U.S. 322 at 325 (1979). Recognition of this principle has given rise to the view that the Commerce Clause, in the absence of evidence of specific action taken by the Federal Government to regulate commerce, nevertheless contains self-executing constraints on state action. *H.P. Hood & Sons, Inc. v. DuMond*, 336 U.S. 525 (1949); *Southern Pacific Co. v. Arizona*, 325 U.S. 761 (1945). In recognition of these self-executing constraints, this Court has developed a species of analysis commonly known as dormant Commerce Clause analysis.

The modern view of dormant Commerce Clause analysis with respect to interstate commerce was set forth in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977), and was extended to foreign commerce, and expanded upon, in *Japan Line, Ltd v. County of Los Angeles*, 441 U.S. 434 (1979). As set forth in *Complete Auto* and *Japan Line*, the elements of a dormant Commerce Clause analysis with respect to foreign commerce are:

1) The tax must be applied to an activity with a substantial nexus with the taxing State, *Complete Auto*, 430 U.S. at 279,

2) The tax must be fairly apportioned, *Id.*,

3) The tax must not discriminate against interstate [or foreign] commerce, *Id.*,

4) The tax must be fairly related to the services provided by the State, *Id.*,

5) The tax must not give rise to an enhanced risk of multiple taxation, *Japan Line* 441 U.S. at 446, and

6) The tax must not impair federal uniformity in an area where federal uniformity is essential. *Id.* at 448.

The capstone decision applying this analysis to taxation of "foreign-source" income is *Container*.

Amici believe that the *Container* decision was correctly decided and controls with respect to the petition of the Colgate-Palmolive Company. Amici also believe that this Court's analysis of the dormant Commerce Clause requirements in *Container*, and in other cases, establishes that application of WWCR to a foreign controlled business is also constitutionally permissible. For purposes of this argument, Amici will apply the Court's dormant Commerce Clause analysis anew to Colgate and to Barclays.

B. The *Complete Auto Transit* Elements

1. Substantial Nexus

The unitary business principle is the linchpin which satisfies the requirements of nexus. *Mobil Oil Corporation v. Commissioner of Taxes*, 445 U.S. 425 (1980); *Container*. This is true for both Due Process Clause and dormant Commerce Clause purposes.

Barclays Bank Limited (Barclays) was present in California in 1977 through a wholly owned subsidiary, Barclays Bank International Limited (BBI), Stip. ¶¶ 1 and 6, BJA-9-10[1], and through a wholly owned second-tier

[1] The Joint Appendix in Barclays is referred to as BJA and the Joint Appendix in Colgate is referred to as CJA.

subsidiary, Barclays Bank of California (Barcal), Stip. ¶¶ 8 and 9, BJA-10-11. Barclays conducted a banking agency business in California, Stip. ¶ 1, BJA-9, and a commercial banking business in California, Stip. ¶ 9, BJA-11. For purposes of this litigation, BBI and Barcal agree that they were members of a worldwide unitary business, within the meaning of California law, conducted by Barclays, Stip. ¶ 27, BJA-16. The nexus element of dormant Commerce Clause analysis is satisfied.[2]

Colgate-Palmolive Company is a corporation organized and existing under the laws of Delaware, was headquartered in New York, and was qualified to do, and was doing, business in California. Stip. ¶ 1, CJA-4. Although at the trial level Colgate contested the Franchise Tax Board's determination that it was conducting a unitary business, it did not appeal the trial judge's adverse decision on this issue. Colgate is a unitary business. The nexus element of dormant Commerce Clause analysis is satisfied for Colgate as well.

2. Fairly Apportioned

In order to prove that the tax determined under an apportionment formula is unfair, the taxpayer must prove "by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportion to the business transacted . . . in that state,' 283 U.S., at 135, [cites omitted] or has 'led to a grossly distorted result,' [Norfolk & Western R. Co. v. State Tax Comm'n, 390 U.S. 317, 326

[2] **Barclays appears to raise the question of whether this issue was decided by the lower courts, Barclays' Brief for Petitioner (Br.Pet.) 13, fn. 6. It does not appear that this has been raised on appeal here, except by Amici Government of the United Kingdom, pp. 24-27.**

(1968)]." *Moorman Mfg. Co. v. Iowa*, 437 U.S. 267, at 274 (1978).

In *Container*, this Court set forth a two-fold standard by which to determine fairness: "internal consistency — that is the formula must be such that, if applied by every jurisdiction, it would result in no more than all of the unitary business' income being taxed" and "external consistency — the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Container*, 463 U.S. at 169. The Court has used this tool to measure the fairness of a state tax in a number of subsequent cases. *Goldberg v. Sweet*, 488 U.S. 252 (1989);[3] *American Trucking Assn., Inc. v. Scheiner*, 483 U.S. 266 (1987); *Armco Inc. v. Hardesty*, 467 U.S. 638 (1984).

California, during the years in issue, followed the UDITPA and used the three-factor apportionment formula contained in the Act for Colgate and used a modified three-factor apportionment formula for Barclays.[4] The use of the three-factor formula was approved by this Court in *Butler Bros. v. McColgan*, 315 U.S. 501 (1942), and is now referred to by the Court as "something of a benchmark against which other apportionment formulas are judged." *Container* 463 U.S. at 170, *Amerada Hess Corporation v. Division of*

[3] The definition of "external consistency" was worded differently in *Goldberg v. Sweet* where the Court phrased it as "ask[ing] whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed." 488 at 262. The difference in wording would appear to have no impact on these cases.

[4] The three-factor formula used by California for banks and financials includes intangible property in the measure of the property factor.

Taxation, 490 U.S. 66 at 73 (1989). UDITPA's apportionment formula is both internally and externally consistent.

During the course of the trial in this matter, counsel for Barclays advised the trial judge that Barclays was not arguing that the taxes were unfairly apportioned. BJA-832-833. The fair apportionment element of dormant Commerce Clause analysis is not at issue in that case.

At the trial level, Colgate argued that application of WWCR distorted the amount of income attributed to California. The trial judge found against Colgate on this issue, and the decision was sustained by the appellate court which held that Colgate had not met the steep burden of demonstrating an unconstitutional distortion of its liability determined through the use of WWCR and that the tax was fairly apportioned. Colgate Petition, Appendix E, pp. 66a-71a. Colgate did not contest the state court decision in its petition to this Court.

3. Discrimination

This Court has held that a tax may violate the Commerce Clause if it is facially discriminatory, has a discriminatory intent, or has the effect of unduly burdening interstate commerce. *Amerada Hess* 490 U.S. at 75.

There is no discrimination on the face of the California statute and neither taxpayer claims that the statute on its face treats in-state and out-of-state businesses differently to the disadvantage of the out-of-state business. There is also no discriminatory intent manifested in the California law, and the taxpayers do not claim that the California tax was intended to give an advantage to local industry.

The only argument offered regarding discrimination is made by Barclays, which argues that the effect of the California tax is discriminatory because it creates undue, "prohibitive," burdens on foreign-based multinational businesses in order to file a California return using WWCR. Petitioner Colgate's argument is even simpler. It is the "What if?" argument. Colgate argues that if this Court were to find in favor of Barclays, regardless of the reason, it would then be discriminatory to tax Colgate under a different taxing scheme.

Stated in its simplest terms, Petitioner Barclays is requesting special treatment because they are foreign-based businesses which voluntarily entered the California market. The Constitution of the United States, the treaties entered into by the United States,[5] and the statutes of the United States do not require that foreign-based businesses be given dispensations so that they may operate at a competitive advantage as compared to United States-based businesses. *Sumitomo Shoji American, Inc. v. Avagliano*, 457 U.S. 176 (1982). A foreign-based business must pay its way, and it is reasonable for a tax authority to require a foreign corporation to present its tax information in a manner which complies with the requirements of the tax authority as long as they do not disadvantage the foreign entity. There is no credible evidence that California's filing requirements cause an undue burden on Barclays. California's rules regarding the preparation of combined reports involving worldwide activities are before

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[5] Barclays' counsel at trial stated that it was <u>not</u> claiming that it had been discriminated against in terms of the protections offered by the United States/United Kingdom Tax Convention. Reporter's Transcript (RT) 1815-1824, BJA-837-840.

this Court, Ex. 12, BJA 50-57, and, therefore, this Court should not be misled by the exaggerated and inaccurate claims made by Barclays and its amici.

First, under California law, it is not necessary for Barclays to set up a second and separate system of accounting. Barclays may use statements it regularly prepares for its own purposes with adjustments to these statements, *if material*, BJA-54, (b)(3)(C), to reconcile differences between foreign and United States GAAP and California tax accounting standards. See Regulation § 25137-6, BJA-50, (b)(A), and BJA-51, (b)(2). Moreover, Barclays had prepared United States GAAP statements for other purposes. Stip. ¶ 51 and Ex. 51G, BJA-40.

Second, Barclays does not have to maintain its records in United States dollars and in English. Regulation § 25137-6 provides that the calculation of income, BJA-51, (b)(1)(D) and (b)(2), and the apportionment factors, BJA-55, (c)(1)(E), and BJA-56, (c)(2)(C), are to be made in the currency of the parent company. In any event, the language in which the consolidated records of Barclays are maintained is English.

Third, Barclays presses the argument that hypothetical costs of compliance in the millions of dollars creates an undue burden and thereby establishes a basis for discrimination which they characterized as "economic protectionism." (Br.Pet. p. 44, fn. 13.) The California appellate court found that the real cost of compliance, as evidenced by the bills from a major accounting firm for preparing the WWCR returns filed by BBI, was $900 to $1,250 annually. Appendix to the Petition, D-19, fn. 9. These returns were acceptable to California except as to the scope of the unitary business. This

Court should defer to the judgment of the California courts as to what level of detail, specificity and documentation is sufficient for California tax filings. This is not the stuff of discrimination.

Fourth, foreign-based businesses do not file on a different basis under Regulation § 25137-6 than do domestic-based businesses, and therefore, the foreign-based businesses need not forgo tax benefits. Barclays' argument is based on the unfounded assumption that a domestic-based business maintains its records in a form which corresponds to the filing requirements of California. The reasons for a domestic-based corporation to maintain records which conform to the requirements of the California Revenue and Taxation Code are the same as they are for a foreign-based corporation: to file California tax returns. There is no other reason. To the extent a separate set of records or schedules is required for a domestic-based business, it is required for a foreign-based business. To the extent a domestic-based business can use estimates and approximations, a foreign-based business may. There is no discrimination. Barclays was treated in the same way every other taxpayer was treated. BJA-831-832.

Finally, Barclays wrongly claims discrimination because it must comply with WWCR in California but domestic-based businesses do not have to comply with WWCR in any foreign country. There is no evidence in the record as to what tax and information requirements domestic-based multinationals are subject to in foreign countries. Without that evidence, Barclays' claim is without support. More importantly, this argument is based on a faulty comparison. The relevant point of comparison for the purposes of the United States Constitution is what *California* requires of domestic-based

unitary businesses versus what it requires of foreign-based unitary businesses. It requires the same method of filing, WWCR, and the same information; therefore, there is no discrimination. In *Container*, this Court, held that the States' use of formulary apportionment need not yield to the arm's-length accounting methods favored overseas. 463 U.S. at 193.

In considering the discrimination arguments raised in these cases, this Court is presented with a blueprint of the consequences if it accepts them. First, Barclays claims discrimination because it is foreign. It advances a number of reasons why its place of organization justifies separate treatment. If this Court accepts Petitioner Barclays' argument, and concludes there is discrimination, then it must face a second claim of discrimination by domestic-based multinationals.

Petitioner Colgate is dependent upon Barclays winning its case. If Barclays does not win, then how can Colgate win? If Barclays is successful, then Colgate argues, as did the dissent in *Container*, 463 U.S. at 197-205, that it is being discriminated against vis-à-vis foreign-based multinationals. Colgate's argument, if accepted, requires that *Container* must be overruled.

The unraveling of the fabric of this Court's analysis continues when Colgate's logic is extended to the unitary business which conducts all or part of its foreign activities through a domestic corporation, or a unitary business which functions through a single corporation, foreign or domestic. Colgate's preferential treatment in these circumstances will again open the door for further claims of discrimination and

the overruling of a series of cases including *Bass, Ratcliff & Gretton, Ltd.*, 266 U.S. 271 (1924), and *Mobil Oil*, 445 U.S. 425. In fact, the consequences may ultimately lead to another revisitation of the unitary business principle as this Court did two terms ago in *Allied-Signal, Inc. v. Director, Division of Taxation*, 504 U.S. ___, 119 L.Ed.2d 533 (1992).

Any differences in compliance costs between domestic-based and foreign-based multinationals argued by Barclays and Colgate are purely hypothetical, not actual, and arise from an improper comparison of taxpayers who are not similarly situated. *Kraft General Foods v. Iowa Dept. of Revenue and Finance*, 504 U.S. ___, 120 L.Ed.2d 59, fn. 23 (1992). By characterizing these hypothetical differences as discrimination, Barclays invites this Court to take a first step on a slippery slope. Barclays has been treated in a nondiscriminatory manner, and the California tax should be affirmed. The question of compliance requirements for similarly situated taxpayers is appropriately left to the legislative branch of government, either state or national, so long as they are fairly applied, as they are here.

4. Fairly Related to Services Provided

The requirements of this element of dormant Commerce Clause analysis are satisfied by the provision of such state services as "police and fire protection, the benefit of a trained work force and 'the advantages of a civilized society.'" *Exxon Corporation v. Wisconsin*, 447 U.S. 207, at 228 (1980). There can be no doubt that both Barclays and Colgate enjoy these basic California benefits and neither petitioner has

presented any evidence with respect to this issue.[6] It is not properly before this Court.

C. The *Japan Line* Elements

This Court's recent comments on the interrelationship between the four elements of the *Complete Auto Transit* analysis and the two *Japan Line* elements should be noted prior to proceeding to an examination of the other two elements of dormant foreign Commerce Clause analysis:

> [C]ompliance with the Complete Auto test has relevance to our conclusion that the state tax meets those inquiries unique to the foreign commerce clause. That the tax is a fair measure of the State's contacts with a given commercial transaction in all four aspects of the Complete Auto test confirms both the State's legitimate interest in taxing the transaction and the absence of an attempt to interfere with the free flow of commerce, be it foreign or domestic. *Itel Containers International Corporation v. Huddleston*, 507 U.S. ___, 122 L.Ed.2d 421, at 436 (1993).

1. Multiple Taxation

In *Japan Line*, this Court first enunciated the "enhanced risk of multiple taxation" element of dormant foreign Commerce Clause analysis. *Japan Line* involved the imposition of a property tax. With respect to property taxes, this Court found that pursuant to the custom of nations, Japan, the country of domicile of the owner of the containers, had asserted property taxes on the full value of the containers (441

[6] Barclays in its petition raises the question as to whether this issue was ruled upon by the trial court. Br.Pet. 13, fn. 6.

U.S. at 454) and therefore the assertion of a tax by Los Angeles would inevitably result in actual multiple taxation (441 U.S. at 455). This Court has had the opportunity to explicate the multiple taxation element of dormant Commerce Clause analysis in subsequent cases.

In *Mobil Oil*, this Court distinguished *Japan Line* as follows:

> That case [Japan Line] involved ad valorem property taxes assessed directly upon instrumentalities of foreign commerce. . . . the factors favoring use of the allocation method in property taxation [taxation in full by the state of domicile] have no immediate application to an income tax. . . . Finally, in Japan Line the Court was confronted with actual multiple taxation that could be remedied only by adoption of an allocation approach. . . . in the present case we are not similarly impelled." 445 U.S. at 448.

In *Itel Containers International Corporation v. Huddleston*, this Court said:

> [T]he foreign commerce clause cannot be interpreted to demand that a state refrain from taxing any business transaction that is also potentially subject to taxation by a foreign sovereign. "Japan Line does not require forbearance so extreme or so one-sided." *Container* [citations omitted] . . . Absent a conflict with a "consistent international practice [or] . . . federal policy" *Container* [citations omitted], the careful apportionment of a state tax on business transactions conducted within state borders does not create the substantial risk of international multiple taxation that implicates foreign commerce clause concerns. 507 U.S.___, 122 L.Ed.2d at 436-437 (1993).

The most thorough explication of the *Japan Line* multiple tax analysis, and the one most directly applicable to the circumstances of these cases, was provided in *Container*, 463 U.S. at 187-193. In *Container*, this Court considered the very method of taxation involved in the present cases and held that what it characterized as actual double taxation was not unconstitutional. In *Container*, 463 U.S. at 187-189, this Court noted four similarities between the circumstances in that case and in *Japan Line*: 1) actual double taxation, 2) a serious divergence in the taxing scheme of California and foreign authorities, 3) a foreign practice consistent with international practice, and 4) a preference for the internationally accepted method by the federal government for purposes of its tax. This Court further noted three differences between the circumstances of *Japan Line* and *Container*: 1) the tax was an income tax not a property tax, 2) the double taxation was not inevitable, and 3) the tax fell not on the foreign owners of an instrument of commerce but on a corporation domiciled and headquartered in the United States. This Court then analyzed the distinctions and determined they constituted a constitutionally significant difference, 463 U.S. at 189. This Court's analysis directs a similar conclusion in these cases.

Colgate and *Container* are identical. The same three distinctions are applicable. Once again, California could achieve the elimination of all double taxation only by deferring to the taxation decisions and income allocation methods made by every other nation. In spite of "double taxation [being] a constitutionally disfavored state of affairs . . . [our analysis] does not require forbearance [by the States] so extreme or one-sided." *Container*, 463 U.S. at 193.

In the circumstances of Barclays, the first two distinctions apply, regardless of the parentage. The tax involved is an income tax where division of the base is the norm, it is not a property tax, and multiple taxation is not automatic.

The clarity and significance of the third distinction is more difficult to determine. In Barclays we have two taxpayers: the first is a California corporation owned by a foreign parent, and the second is a foreign incorporated entity doing business in California.[7] The facts of this case demonstrate that no significance should be attached to ownership. First, the taxpayers are amenable to being taxed in some manner. Second, the only manner of avoiding any complaints is to forgo taxation completely or to have it dictated by the foreign countries. Third, almost seventy years ago this Court accepted the proposition that a foreign-country-domiciled taxpayer could have its State income determined under a formulary method. *Bass, Ratcliff & Gretton, Ltd v. State Tax Commission*, 266 U.S. 271 (1924). No circumstances are presented in this case which justify this Court abandoning this long-established precedent.

2. One Voice

As an initial matter, this analysis must start with the admonition of this Court that "Absent some explicit directive from Congress, we cannot infer that treatment of foreign income at the federal level mandates identical treatment by the States." *Mobil Oil*, 445 U.S. at 448. In light of this

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[7] In *Container*, this Court noted that a different level of significance might attach to the incident of the tax when the taxpayer was owned by foreign interests. The Court did not determine whether this would be analytically significant. 463 U.S. at 195, fn. 32.

admonition, the fact that the Federal Government uses the arm's-length method does not automatically require the States do so.

The Executive and Legislative branches have determined that this is not an area where it is *essential* for the Federal Government to speak with one voice. Their judgment has proven correct.

Japan Line stated that an element of the dormant Commerce Clause test is whether the state tax "may impair uniformity in an area where federal uniformity is essential." 441 U.S. at 448. The determination of whether a particular area is one where uniformity is *essential* must in the first instance be a determination to be made by the Legislative Branch which is vested by the United States Constitution with the authority to regulate Commerce. (U.S. Const., art. I, § 8, cl. 3.) As this Court has recognized, it "has little competence in determining precisely when foreign nations will be offended by particular acts, and even less competence in deciding how to balance a particular risk of retaliation against the sovereign right of the United States as a whole to let the States tax as they please." *Container*, 463 U.S. at 194.

The determination that this is an area where uniformity is not essential has been made by the Congress as evidenced by 1) the action of the United States Senate in refusing to give its advice and consent to a United States/United Kingdom Tax Convention containing a restriction on state taxation specifically intended to prohibit the tax here at issue, Ex. 36C, BJA-238 and Ex. 36D, BJA-311, 2) the Senate's approval of treaties containing no limitation on the States' use of WWCR both in conjunction with, and subsequent to, the United

States/United Kingdom Tax Convention, Stip. ¶ 40, BJA-26-31, and 3) Congressional failure to enact numerous bills which would have prohibited the State tax here at issue, Stip. ¶ 38, BJA-24-25. Of particular significance in the latter regard are the bills which were introduced and considered after the Senate's rejection of the United States/United Kingdom Tax Convention. There could be no doubt what was at stake with respect to those bills, yet no action was taken. Even if the Court is unwilling to consider these actions as an affirmative act of the Congress which would completely preempt a dormant Commerce Clause analysis (see *Western and Southern Life Insurance Company v. State Board of Equalization*, 451 U.S. 648 (1981)), they are, nonetheless, sufficient to establish a Congressional determination that this is an area where federal uniformity is not essential.

Further evidence of the determination that this is an area where federal uniformity is not essential is supplied by the actions of the Executive Branch in years subsequent to the Senate's rejection of the United States/United Kingdom Tax Convention by its request for voluntary state action, its withdrawal of support for a federal legislative solution, Ex. 37I, BJA-439, and its determination that this Court need not consider the petition filed by Barclays in the instant case. Brief of United States, October 7, 1993.

This Court's one-voice analysis in *Container* also took into consideration whether a state tax "might *justifiably* lead to significant foreign retaliation." (Emphasis added.) 463 U.S. at 194. Retaliation in unlikely here. The treaty negotiated between the United Kingdom and the United States, as ultimately approved by the Senate, does not prohibit the tax here at issue. Ex 36D, BJA 393-394. In fact, the United

Kingdom and the United States negotiated additional concessions as the result of the Senate's refusal to give its advice and consent to the restriction the UK sought. Third Protocol to the Treaty, Ex 37H, BJA-436. Finally any retaliation of the sort the British have threatened has been recognized by the Executive Branch as a violation of the treaty now in effect. Testimony of Roger Mentz, Ex 37I, BJA 439 at 443.

In *Container*, this Court was faced with having to determine whether the state tax could interfere with United States foreign policy without the benefit of a fully developed history such as is present in this case. To assist in its determination, this Court made reference to three "objective standards that reflect very general observations about the imperatives of international trade and international relations." 463 U.S. at 194.[8] In the circumstances of these cases, there is no need for this Court to engage in this complex, technical and somewhat speculative analysis because other facts and circumstances have established that uniformity is not essential. More importantly, several United States Senators have filed an *amicus* brief in support of California in this case requesting that this Court leave complex foreign policy analyses to the Senate.

[8] For example, this Court in *Japan Line*, 441 U.S. at 453, discussed the "asymmetry" of California's tax. There "asymmetry" referred to the fact that Japan did not tax American containers at all, while Los Angeles County wished to tax Japanese containers in part. Petitioner Barclays reads this to mean that because it believes no other jurisdiction, other than a State, uses WWCR there is "automatic asymmetry." Br.Pet. pp. 28-29. If Barclays' definition were correct, then "automatic asymmetry" would exist in *Container*, but this Court found it did not. 463 U.S. at 194-195. Therefore, Barclays' interpretation of "automatic asymmetry" is incorrect.

D. Consistency is Very Important in State Taxation

This Court's decision in *Container* has been the rule of law for over ten years. Congress has certainly had the power to change the result of that decision and has not done so. Overturning the *Container* decision would almost certainly impact the taxation of multinational corporations by the vast majority of the States that use the formulary apportionment principles of UDITPA.[9] *See Moorman Mfg. Co.*, 437 U.S. at 283, fn. 1 (Powell, J. diss.). Each of these States that utilize UDITPA to apportion income has relied on and applied *Container* to the thousands of corporations with multinational income doing business in their States. With multi-year refunds available, a reversal of *Container* will result in a tremendous assault on the States' current revenues. *See Harper v. Commonwealth of Virginia*, 507 U.S.___ , 125 L.Ed.2d 74 (1993).

Therefore, while California's taxing system passes every element of dormant Commerce Clause analysis, the taxes can and should be upheld by this Court also on the basis of *stare decisis*. In *Quill Corporation v. North Dakota*, 504 U.S. ___, 119 L.Ed.2d 91 (1992), this Court offered the following comments with respect to its Commerce Clause-based cases:

> [T]he Bellas Hess rule appears artificial at its edges: . . . This artificiality, however, is more than offset by the benefits of a clear rule. Such a rule firmly establishes the boundaries of legitimate state authority. . . . This benefit is important, for as we have so frequently noted, our law in this area is something of a "quagmire" and the

[9] Forty-five of fifty states (all which assert taxes on or measured by income) use some form of apportionment.

"application of constitutional principles to specific state statutes leaves much room for controversy and confusion and little in the way of precise guides to the States in the exercise of their indispensable power of taxation." Northwestern States Portland Cement Co. v. Minnesota [cites omitted].

. . . [A] bright-line rule . . . encourages settled expectations and, in doing so, fosters investment by business and individuals. 119 L.Ed.2d at 109.

CONCLUSION

The "proper and fair method of taxation," *Container*, 463 U.S. at 184, used by California in these cases passes all elements of a dormant Commerce Clause analysis and is a constitutional exercise of California's sovereign power to tax. The judgments of the California courts should be affirmed.

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Respectfully submitted,

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